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Ontario Energy Board



Ontario

IN THE MATTER OF THE
ONTARIO ENERGY BOARD ACT
RESPECTING

AN APPLICATION BY
CARDINAL POWER, L.P.
FOR A BYPASS COMPETITIVE RATE
WITH CENTRA GAS ONTARIO INC.

E.B.R.O. 477

DECISION WITH REASONS

May 27, 1993

Pour des renseignements en français, veuillez communiquer
avec la Commission de l'énergie de l'Ontario.

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à frais virés.)

Ontario Energy Board



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EXECUTIVE SUMMARY
ONTARIO ENERGY BOARD
E.B.R.O. 477 DECISION DATED MAY 27, 1993

Cardinal Power of Canada, L.P. filed an application dated February 10, 1992, as amended on August 28, 1992 (the Rate Application), with the Ontario Energy Board under section 19 of the *Ontario Energy Board Act*. Cardinal Power requested an order fixing or approving a just and reasonable rate for the transportation of gas by Centra Gas Ontario Inc. from the transmission system of TransCanada PipeLines Limited to a cogeneration facility to be owned and operated by Cardinal Power in the Village of Cardinal. The Rate Application was an alternative to three other applications dated February 10, 1992 under the Act and the *Municipal Franchises Act* (Board File Nos. E.B.L.O. 242, E.B.C. 198 and E.B.A. 627) that sought to give authority to Cardinal Power to construct and operate its own pipeline (the Pipeline Application).

Cardinal Power is a limited partnership between Husky Oil Limited of Calgary, Alberta and Sithe/Energies of New York, New York. It was formed to design, construct, own and operate a cogeneration plant located at the Canada Starch Company in Cardinal, Ontario. The Village of Cardinal is located near Cornwall and is presently served by Centra.

Cardinal Power and Centra entered into an agreement by a letter dated June 24, 1992 providing for transportation service to the cogeneration facility. The agreement was based on a minimum annual volume of 287,000 10^3m^3 . The parties agreed to a ten-year term and a bypass competitive rate of \$4.80 per 10^3m^3 fixed for the primary term of five years.

Based on a reading of past Board decisions, it appeared that a three-part test had evolved for the purpose of assessing an application for a bypass competitive rate:

- Q1. Is the applicant for a bypass competitive rate a credible candidate for a bypass?
- Q2. Is it in the public interest to grant a bypass competitive rate?
- Q3. Is the proposed rate just and reasonable?

In this Decision, the Board did not approve a bypass competitive rate for Cardinal Power as it did not pass the three-part test. Although Cardinal Power may be a credible bypass candidate (Q1), the Board was not satisfied that it was in the public interest to grant this special rate to the Applicant under the circumstances (Q2). Because approval was not granted, there was no need to address the appropriateness of the proposed rate (Q3).

The Board heard that there was a certain level of discontent with the present structure of Centra's Rate 20. The Board noted that Centra had filed its 1994 rates application (Board File No. E.B.R.O. 484), and had included a proposal to create a high volume, high load factor rate class. If the proposal is accepted by the Board, customers like Cardinal Power may observe some rate relief.

E.B.R.O. 477

IN THE MATTER OF the Ontario Energy Board Act,
R.S.O. 1990, Chapter O.13;

AND IN THE MATTER OF an amended application by
Cardinal Power of Canada, L.P. to the Ontario Energy
Board pursuant to Section 19 of the Ontario Energy
Board Act, for an order or orders fixing the just and
reasonable rate that Centra Gas Ontario Inc. may charge
to Cardinal Power of Canada, L.P. for services related to
the supply of natural gas to Cardinal Power of
Canada, L.P. at Cardinal Power of Canada L.P.'s plant
located in Cardinal, Ontario.

BEFORE: E.J. Robertson
Presiding Member

Pamela Chapple
Member

C.L. Cottle
Member

DECISION WITH REASONS

May 27, 1993

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1. **INTRODUCTION**

1.1 **THE APPLICATION**

1.1.1 Cardinal Power of Canada, L.P. ("Cardinal Power" or "the Applicant") filed an application dated February 10, 1992, as amended on August 28, 1992 ("the Rate Application"), with the Ontario Energy Board ("the Board") under section 19 of the *Ontario Energy Board Act* ("the Act"). The Applicant requested an order fixing or approving a just and reasonable rate for the transportation of gas by Centra Gas Ontario Inc. ("Centra") from the transmission system of TransCanada PipeLines Limited ("TCPL") to a cogeneration facility to be owned and operated by Cardinal Power in the Village of Cardinal. The Rate Application was an alternative to three other applications dated February 10, 1992 under the Act and the *Municipal Franchises Act* (Board File Nos. E.B.L.O. 242, E.B.C. 198 and E.B.A. 627) that sought to give authority to Cardinal Power to construct and operate its own pipeline ("the Pipeline Application").

1.1.2 The Applicant's evidence in this matter consisted of material filed both with the Rate Application and with the Pipeline Application (including the responses to interrogatories). Centra filed evidence in support of the Rate Application, and both the Applicant and Centra jointly sponsored an expert witness, whose evidence was filed in January, 1993.

1.2 THE HEARING

1.2.1 By a Notice of Hearing dated February 9, 1993, the Board appointed February 23, 1993 for the commencement of the hearing. The hearing lasted for four days, not including the procedural day to hear motions on February 15.

1.2.2 The following is a list of the parties and their representatives:

Cardinal Power	Lawrence Smith Peter Budd
Centra	Michael Penny
Board Staff	John Campion
Industrial Gas Users Association ("IGUA")	Peter Thompson
Northland Power ("Northland")	Dan Sinclair
The Consumers' Gas Company Ltd. ("Consumers Gas")	Barbara Bodman
Destec Energy Canada ("Destec")	Michael Meacher
Independent Power Producers Society of Ontario	Tom Brett
Union Gas Limited	Michael Verwegan

1.2.3 The following witnesses testified on behalf of the Applicant:

Michael Crough	Vice-President, Business Development, Sithe Energies, Inc.
Robert Thompson	Project Development Manager, Husky Oil Ltd.

1.2.4 The following witness testified on behalf of the Applicant and Centra:

Malcolm Jackson	President, Financial Regulatory Consultants of Canada
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1.2.5 The following Centra employees testified on behalf of Centra:

Keith Bryan	Manager, Regulatory Projects and Research
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Patrick Hoey	Manager, Regulatory Affairs
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1.2.6 The following witness testified on behalf of IGUA:

Ted Bjerkelund	Executive Director, IGUA
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1.2.7 The Applicant delivered oral argument on February 26, 1993 and Centra filed written argument on March 3. Board Staff, IGUA and Northland filed their written arguments on March 10 and both the Applicant and Centra filed reply argument on March 15, 1993.

1.2.8 Copies of the prefiled evidence and exhibits in this proceeding, together with a verbatim transcript, are available for public examination at the Board's offices. The Board has considered all the evidence, submissions and arguments presented in this proceeding. The following is a summary of the evidence and positions necessary to clarify the issues.

DECISION WITH REASONS

2. BYPASS COMPETITIVE RATE

2.0.1 The Board reviewed the following Board decisions on bypass, and relative to that, bypass competitive rates:

- the Bypass Decision under Board File Nos. E.B.R.O. 410-I, 411-I, 412-I (dated December 12, 1986);
- the T-Rates Decision under Board File Nos. E.B.R.O. 410-II, 411-II, 412-II (dated March 23, 1987);
- the decisions dealing with applications for a bypass competitive rate:

E.B.R.O. 435	- Cyanamid (dated July 9, 1987);
E.B.R.O. 430-2B	- Nitrochem (dated May 20, 1988);
E.B.R.O. 411-III et al.	- Algoma and Domtar (dated May 20, 1988);
E.B.R.O. 457	- C-I-L (dated December 1, 1989);
E.B.R.O. 458	- Northland (dated May 24, 1990);
E.B.R.O. 461	- Algoma (dated May 22, 1991); and
E.B.R.O. 471	- CP Forest (dated August 27, 1991);

- the Decision dealing with Centra's proposed cogeneration rate class under Board File No. E.B.R.O. 467 (dated May 22, 1991).

2.0.2 Based on a reading of these decisions, it appears that a three-part test has evolved for the purpose of assessing an application for a bypass competitive rate.

- Q1. Is the applicant for a bypass competitive rate a credible candidate for a bypass?
- Q2. Is it in the public interest to grant a bypass competitive rate?
- Q3. Is the proposed rate just and reasonable?

2.0.3 The Board views the answer to this first question as fundamental to an application for a bypass competitive rate. The notion of credibility suggests that to justify an action that goes against the norm (i.e., class ratemaking and postage stamp rates¹) there must be a threat that the system may lose the existing or a new load because the customer may go out of business, use a substitute for natural gas, or physically bypass the local distribution system entirely by building its own pipeline. If the customer-applicant is not a credible bypass candidate, then there is no threat of loss and, therefore, no competitive justification for the rate. On the other hand, if the applicant is credible, there may be both a threat of loss to the system and the justification for a bypass competitive rate.

2.0.4 The Board notes that an applicant that establishes itself as a credible bypass candidate cannot be assured that a bypass competitive rate will be subsequently approved. All rates, including bypass competitive rates, must, generally, be in the public interest and, specifically, be just and reasonable. In the same way, an applicant that establishes itself as a credible bypass candidate in an application for a bypass competitive rate is not automatically guaranteed that approval would be forthcoming in an application for a physical bypass. The Board must be satisfied that a

¹ Postage stamp rates are uniform in a specified area and are charged on a volumetric basis regardless of distance.

bypass meets a number of concerns (eg., landowner and environmental interests), as well as being in the public interest.

- 2.0.5 In this Decision, the Board does not approve a bypass competitive rate for Cardinal Power as the Applicant did not pass the three-part test. Although Cardinal Power may be a credible bypass candidate (Q1), the Board is not satisfied that it is in the public interest to grant this special rate to the Applicant under the circumstances (Q2). Because approval is not being granted, there is no need to address the appropriateness of the proposed rate (Q3).

DECISION WITH REASONS

3. BACKGROUND

3.0.1 Cardinal Power is a limited partnership between Husky Oil Limited of Calgary, Alberta ("Husky Oil") and Sithe/Energies of New York, New York. It was formed to design, construct, own and operate a cogeneration plant located at the Canada Starch Company ("CASCO") in Cardinal, Ontario. The Village of Cardinal is located near Cornwall and is presently served by Centra.

3.0.2 The capital cost to construct the cogeneration facility is estimated to be \$170 million. The debt component of Cardinal Power's capital structure is estimated to be 85 percent (as amended from the original 80 percent). Construction financing for the project was completed on September 30, 1992 and will be converted to term financing when construction is completed. Term financing is conditional upon economic forecasts that will yield a cash flow providing adequate coverage for the payment of interest and principal over the term of the loan. The financing is non-recourse debt financing, namely, the lenders have no recourse to the sponsors of the project. As of January 1993 the Applicant had spent \$36 million on the project.

3.0.3 At the time of the hearing, the construction of the cogeneration plant had commenced; it is expected to be in commercial operation by July 1994. The cogeneration plant is forecast to produce 150 megawatts of electricity

for sale to Ontario Hydro and 65,000 pounds per hour of steam for CASCO's use in processing. The cogeneration plant will displace some gas load currently delivered to CASCO by Centra.

- 3.0.4 Cardinal Power has a 20 year Power Sale Agreement with Ontario Hydro for the sale of its electricity, which is its primary revenue source, and a steam sale agreement with CASCO. The agreement with Ontario Hydro includes levelizers that smooth out the revenue payments from Ontario Hydro. Under these arrangements, "the point of greatest project vulnerability" will occur approximately ten years after the plant is operational.
- 3.0.5 Cardinal Power will purchase natural gas for its use at the cogeneration plant from Husky Oil and Husky Oil has arranged transportation service with TCPL. The gas purchase agreement provides for a natural gas supply warranted by Husky Oil and the gas price is directly (and directionally) linked to changes in the price that the Applicant receives from Ontario Hydro under the Power Sale Agreement.
- 3.0.6 A new pipeline between the TCPL transmission line and the cogeneration facility is required to serve the facility. Initially Cardinal Power made its Pipeline Application to own, build and operate that pipeline itself. The Rate Application was held in abeyance pending the outcome of the Pipeline Application. The hearing on the Pipeline Application was scheduled to commence on July 7, 1992. By a letter to the Board dated June 26, 1992, Cardinal Power requested that the hearing of the Pipeline Application be adjourned to enable it to proceed with the Rate Application, as the Applicant had reached a conditional understanding on a bypass competitive rate with Centra.
- 3.0.7 Centra's large industrial customers are provided firm or combined firm and interruptible delivery services under Rate 20. A customer is only eligible for Rate 20 if its total maximum daily requirement is $28 \times 10^3 \text{ m}^3$ or more.

The 100 percent load factor delivery rate for Rate 20 approved in E.B.R.O. 474 is \$8.30 per 10^3m^3 ; with Cardinal Power as a Rate 20 customer, the 100 percent load factor rate would decrease to \$7.64 per 10^3m^3 ; with Cardinal Power paying the proposed bypass competitive rate, the 100 percent load factor rate would decrease to \$7.76 per 10^3m^3 .

3.0.8 Cardinal Power and Centra entered into an agreement by a letter dated June 24, 1992 providing for transportation service to the cogeneration facility. The agreement was based on a minimum annual volume of 287,000 10^3m^3 . The parties agreed to a ten-year term and the rate applicable to the service for the primary term of five years.

3.0.9 The Applicant proposed a bypass competitive rate of \$4.80 per 10^3m^3 . Based on the proposed rate, the annual delivery cost for this gas is about \$1.4 million, compared to the cost of \$2.2 million that would be charged if Cardinal Power was a Rate 20 customer. The bypass competitive rate is higher than the estimated effective cost of a pipeline constructed, owned and operated by the Applicant. The estimated cost of transmission under a physical bypass scenario is \$2.03 per 10^3m^3 , for a total annual cost of \$583,000. This figure does not include a provision for load balancing costs that may be required, nor does the proposed bypass competitive rate; Rate 20, however, does include the cost of load balancing.

3.0.10 Following the agreement with Cardinal Power for a special rate, Centra filed an application, dated August 31, 1992, for a leave to construct a pipeline and related facilities in the Village of Cardinal and the Township of Edwardsburgh, "in the event that Centra and Cardinal Power enter into an agreement for the distribution of gas by Centra to Cardinal Power as contemplated in the pending application of Cardinal Power in E.B.R.O. 477". This application has been given Board File No. E.B.L.O. 245.

DECISION WITH REASONS

4. **IS THE APPLICANT A CREDIBLE CANDIDATE FOR A BYPASS?**

Positions of the Parties

4.0.1 The following submissions were made by the parties to support the credibility of Cardinal Power to finance, construct, own and operate a pipeline, (i.e., a physical bypass).

- Cardinal Power evidenced its intent to physically bypass by filing its Pipeline Application. It submitted that it is prepared to proceed with the Pipeline Application should the Rate Application be denied.
- Cardinal Power had dealt with many of the matters related to the construction of the bypass pipeline, including land and environmental matters, in the Pipeline Application.
- Since there are no existing facilities and, therefore, no duplication of facilities, Cardinal Power submitted that its status as a credible physical bypass candidate is enhanced.
- Centra found the Applicant's estimated cost to construct to be credible.

- Cardinal Power has the financial resources to proceed with the construction of the bypass pipeline.
- The cogeneration facility is located in close proximity (approximately 6.8 kilometres) to the TCPL transmission line.
- Cardinal Power will be a large volume user (minimum annual volume 287,000 10³m³), operating at a high load factor (approximately 90%).
- There is an economic advantage to a physical bypass for Cardinal Power; the costs of serving itself are lower than Centra's Rate 20, an estimated difference of \$1.6 million annually. The estimated difference between the costs of serving itself and the proposed rate is \$0.8 million annually.
- Husky Oil, one of the partners, as the owner and operator of gas pipelines, has engineering, technical and construction expertise in pipeline construction and operation.
- Husky Oil will also supply the gas to the project. It has secured the necessary arrangements on the NOVA Corporation of Alberta and TCPL systems.
- Cardinal Power is located in close proximity to the United States and to the Iroquois pipeline into the United States. The Applicant insinuated that there might be an international physical bypass alternative to Centra's service.

4.0.2

Cardinal Power contended that it filed the Pipeline Application because it believed that the ownership and operation of its own line would allow it to control its gas service and gas costs. It argued that it was pursuing the bypass competitive rate as a compromise, and believed the proposed rate to be an acceptable middle ground for all parties. Cardinal Power

maintained that it has the resolve, intent and ability to pursue the Pipeline Application if its Rate Application is not approved; it stated that it "has a very strong economic incentive to pursue bypass options, be it via a rate settlement or a physical bypass." The Applicant submitted that this would include any international bypass option. Although it was not the shortest bypass alternative, Cardinal Power claimed that the current level of Rate 20 provided considerable latitude to consider the more expensive international option.

- 4.0.3 There was very little disagreement amongst the parties as to the credibility of the Applicant to finance, construct, own and operate a pipeline, as described in the Pipeline Application.

Board Findings

- 4.0.4 The Board finds that Cardinal Power exhibits the necessary characteristics to be considered a credible physical bypass candidate in that it could, if authority were to be ultimately granted, finance, construct, own and operate a domestic pipeline, which would result in a physical bypass of Centra, the local distribution company ("LDC"). The Board does not accept, however, the size of the economic advantage attributed to Cardinal Power serving itself as there has been no testing of the costs of supplying gas to meet the needs of the cogeneration operation, including load balancing costs.
- 4.0.5 Although there was some reference to an international physical bypass pipeline under the St. Lawrence River, this notion was not tested in these proceedings. The Board does not have the evidence before it to judge an international physical bypass to be a real threat at this time. The Board agrees with IGUA that if circumstances change and the Applicant has evidence to convince the Board that it is a credible international bypass candidate, then Cardinal Power could consider reapplying for rate relief on the basis of costs associated with the international alternative.

DECISION WITH REASONS

**5. IS IT IN THE PUBLIC INTEREST TO GRANT A BYPASS
COMPETITIVE RATE?**

Positions of the Parties

Cardinal Power

- 5.0.1 The Applicant maintained that it is in the public interest that the Board approve a bypass competitive rate for Cardinal Power.
- 5.0.2 Cardinal Power submitted that a gas user is motivated to consider a bypass in order to reduce costs or to improve its situation. It explained that the motivation behind the Rate and Pipeline Applications is to keep costs down and economic risk under control. In its attempt to achieve that end, the Applicant further explained that it is assisted in this respect by the presence of a competitive alternative to the traditional way of transporting gas, namely, a physical bypass of the LDC. The Applicant submitted that the merits of the proposed rate should be measured against that competitive alternative, namely, that Cardinal Power would not be on the Centra system. The Applicant argued that its resolve, intent and ability to pursue bypass options are evidence of a real possibility that Centra could lose the Cardinal Power load. The Applicant submitted that as long as it is paying Rate 20, there would be an incentive to bypass; "that could happen in year five as easily as it could happen today." A more moderate

solution to the Applicant's problem of cost control and risk minimization would be a rate that can compete with bypass, namely, the proposed rate, which is the subject of this proceeding.

5.0.3 The Applicant defined the real cost of the transportation service that it requires to be about 25 percent of the Rate 20 charge. Although the proposed rate does not solve the Applicant's problem in total by reducing the cost of the service down to the real cost, it explained that a bypass competitive rate does ameliorate the problem.

5.0.4 Cardinal Power explained that there are risks attached to the project, and should they occur the project could be in trouble. Because its revenue stream is fixed, it described why it is necessary to look at the cost-side of the project to build in protections. It submitted that its economic need to control costs and minimize risk by obtaining more competitively priced transportation arrangements would "best position it for long-term viability". When a witness for the Applicant was asked what was the most compelling reason for approval of the proposed rate, he testified that,

... [a bypass competitive rate] gives the strength, the financial strength, the resilience for the project that it wouldn't have at the Rate 20 level and that that resilience to the project give us a little more ability to withstand some of the difficulties. It makes a stronger project, it makes it all the more likely that we will endure for the 20 years and deliver the benefits we expect.

5.0.5 The Applicant suggested that any cost above the real cost is an "overcontribution". Using the proposed rate the Applicant submitted that Centra's other ratepayers would benefit by a contribution from Cardinal Power of approximately \$1 million. The 100 percent load factor rate for Rate 20 customers would reduce from \$8.30 per 10^3m^3 to \$7.76 per 10^3m^3 . In addition, there would be an assurance of a long-term contribution to Centra as there are minimum revenues over the term of the ten-year contract. On the other hand, if Cardinal Power is not on the system, there

will be no contribution to the Centra system and no benefits to the system users.

- 5.0.6 The Applicant submitted that there is a negative impact on the public interest where there is cost shifting from an existing customer to other customers. The Applicant argued that because the load in this instance is incremental, there is no cost shifting, and that because there is no cost shifting, there is no negative impact to overcome in this case. Cardinal Power suggested that where the load is incremental the practical onus imposed on an applicant to prove its case is less onerous than where there is cost shifting. The Applicant also submitted that other customers of Centra will not bear a real cost if the Applicant does not pay the class rate, as it is not at present paying Rate 20.

Centra

- 5.0.7 Centra identified six factors that it uses to determine whether or not to enter negotiations with a customer for a bypass competitive rate: the location of the customer in relation to TCPL; impediments to construction between the customer and TCPL; the size and characteristics of the customer's gas needs; customer access to financial and technical resources necessary to construct the pipeline; arrangements made to obtain TCPL capacity and load balancing capability; and lastly, acceptance of the responsibility for the rates application through the regulatory process. The combination of these factors must convince Centra that it is feasible and economically advantageous for the customer to build and operate its own pipeline instead of using the Centra system. The customer must also provide engineering data and cost information relating to the physical bypass; Centra uses this information in its determination of the rate. Further, if the customer is a cogeneration customer, Centra requires that there be a signed power purchase contract with Ontario Hydro that has received Lieutenant Governor in Council approval. Centra submitted that the physical bypass alternative is to be assessed on the basis of the

economics of the bypass pipeline, not on the basis of the economics of the entire project.

- 5.0.8 Based on the above considerations, Centra entered into negotiations with Cardinal Power. It submitted that it believed there was a "very real risk" that the Applicant would be lost as a customer on the system as the posted rates were higher than the costs to Cardinal Power of serving itself, and the loss was considered to be "a very serious threat to our business". Therefore, Centra followed Board dictates from past decisions to look at ratemaking solutions to bypass, and negotiated the proposed rate.
- 5.0.9 Since the proposed rate will exceed the incremental cost to Centra of serving the Applicant, Centra argued that it and its customers will be significantly better off with Cardinal Power on the system paying the bypass competitive rate than off the system and making no contribution to the system. Further, if Centra builds the pipeline there are four potential customers who could be added immediately and security of supply to existing customers will be enhanced. Centra submitted there is no shifting of costs because the load is incremental. Centra explained that the proposed rate includes a contribution to operating, maintenance and administration costs, which will work to the benefit of other Rate 20 customers. In addition, the rate is a demand charge, which is fixed regardless if the volumes actually taken are lower than the forecast amount. This represents an ensured revenue stream for Centra for ten years. If the system is bypassed, Centra submitted that these benefits would not accrue and there would be detrimental effects: the deliveries to CASCO would be lost and there would be no margin from Cardinal Power to replace this lost portion of the CASCO load; there would be no contribution from Cardinal Power to the system as a whole; and the Rate 20 charge would not decrease. For all these reasons, Centra submitted that a bypass competitive rate for Cardinal Power is in Centra's interests and the interests of its customers.

Board Staff

- 5.0.10 Board Staff could not identify any economic hardship being endured by the Applicant. In fact, as pointed out by Board Staff, Cardinal Power testified that it used Rate 20 in its economic analyses that supported the project, including those relating to long-term profitability, and met its hurdle rate of profitability using Rate 20. The Applicant stated that the project is economically feasible and it will proceed with or without Rate 20. Board Staff also could not find any evidence of competitive pressures in the Applicant's market to support a special rate.
- 5.0.11 In Reply, the Applicant maintained that economic hardship is not determinative on its own or relevant in all situations. It argued that the determinative criterion in this instance is "the existence of a competitive economic alternative to taking service from the LDC and the bypass credibility of the applicant." Cardinal Power went on to suggest that the utility and its customers now face an economic threat because of the potential for a physical bypass. The Applicant also maintained that the economics of a bypass are relevant, and not those applying to the customer's business. The Applicant noted that Board Staff ignored the competitive pressures that Cardinal Power could face on a prospective basis. Moreover, Cardinal Power submitted that it faces strong and significant competitive pressures in its need for cost control through both the construction and the operation phases, and with respect to maintaining its narrow operating margin and debt coverage subsequent to start-up of the operations.
- 5.0.12 Board Staff identified Cardinal Power's "problem" as a desire to achieve cost savings. It appeared as if the purpose of the special rate was solely to reduce costs. In Board Staff's estimation the savings would have a minimal impact on the risk factors influencing future cost control and the remaining risk is not of sufficient magnitude to justify a departure from the class rate. Board Staff likened the cost savings to profit enhancement.

With respect to concerns regarding the future financial performance due to the nature of the agreement with Ontario Hydro, decreased margins, and expected decreases in debt coverage capacity, Board Staff submitted that special treatment should not be granted at this time "because of uncertain future events, especially when under the Applicant's own analysis the project will be viable over its 20-year expected life even assuming Rate 20."

- 5.0.13 In Reply, the Applicant asserted that following Board Staff's reasoning would result in the Board regulating the profit of the utilities' customers under its mandate to set just and reasonable rates for the utilities. Further, it contended that this line of reasoning is similar to that on economic hardship, which it submitted is neither relevant nor probative.
- 5.0.14 Board Staff submitted that the principle of utility regulation in Ontario rests on postage stamp rates and such rates reflect the overall public interest. Board Staff argued that the answer to the public interest question depends on whether Cardinal Power has presented appropriate and compelling reasons to deviate from postage stamp rates. Board Staff submitted that Cardinal Power did not provide reasons to warrant a deviation, and, therefore, a bypass competitive rate for Cardinal Power was not in the public interest. In Reply, Cardinal Power indicated that the existence of a competitive alternative to the LDC is the reason for the Rate Application. Further, it maintained that there is no evidence that the Applicant would become a "committed" user of the Centra system if the proposed rate was not approved, and so there is the possibility that the entire contribution to other customers could be lost.
- 5.0.15 Board Staff submitted that the fact that the Applicant is an incremental customer is not relevant. In Board Staff's view, the principles for eligibility should be the same for existing and incremental customers, otherwise inappropriate intergenerational discrimination would result. The Applicant did not disagree with Board Staff's position. In its Reply,

however, the Applicant suggested that it might be easier for an incremental customer to satisfy the public interest considerations for a bypass competitive rate than for an existing customer. Further, it submitted that if the same rules are applied to existing and incremental customers and intergenerational discrimination results, then intergenerational discrimination would be appropriate. Moreover, Cardinal Power argued that arguments on intergenerational discrimination should be based on evidence in the proceeding, of which, it suggested, there was none.

- 5.0.16 Board Staff disagreed with the Applicant's designation of the payment of Rate 20 being above the "real cost" as an "overcontribution". Board Staff submitted that any person who pays less than the class rate is in fact "undercontributing" to the system.

IGUA

- 5.0.17 IGUA submitted that authority to construct and operate a bypass pipeline or the approval of a special bypass competitive rate should be granted "very sparingly" and should be the "regulatory choice of last resort". IGUA submitted that the evidence surrounding the key principles enunciated in the CP Forest Decision - class ratemaking is preferable and public interest considerations - lead to the conclusion that it is not in the public interest to grant a special rate to Cardinal Power.
- 5.0.18 With respect to private interest facts, IGUA agreed that there will be savings, but these are not significant, amounting to about two percent of the Applicant's total annual cost of operations. IGUA argued that a special rate does little to assist the Applicant in controlling its overall costs. Also a special rate is not needed to justify the economic feasibility of the cogeneration project since Cardinal Power has a 20-year power sale agreement and non-recourse debt financing based on Rate 20.

- 5.0.19 In its discussion of public interest considerations, IGUA addressed: the non-distinguishing features of Cardinal Power compared to other customers of Centra; the lack of economic threat; cost shifting implications; the economic feasibility and long-term competitiveness of Cardinal Power; estimated returns to project sponsors; industrial development; special rates as a surrogate for a competitive delivery system; and implications for other customers. IGUA submitted that there is no real likelihood that the project will not proceed if the proposed rate is not approved nor that the Applicant will decline to take service from Centra.

Northland

- 5.0.20 Northland submitted that the test for a bypass competitive rate should be whether the applicant will contribute more toward the utility's revenue requirement than would be the case if it left or refused to join the system as a Rate 20 customer. Because Centra would receive \$1 million of revenue through the proposed rate when compared to the bypass alternative, Northland argued that Cardinal Power passed the test and the Rate Application should be approved.

Board Findings

- 5.0.21 Having found the Applicant to be a credible bypass candidate, then the second question must be dealt with: Is it in the public interest to grant a bypass competitive rate? It may well be that the construction of a bypass pipeline, and thus, the approval of a bypass competitive rate, would be in the Applicant's private economic interest. But would a bypass competitive rate, the subject of this Decision, be in the public interest?
- 5.0.22 The public interest is an overriding consideration in an application by a customer (either existing or incremental) for a special rate. The Board must weigh all interests to determine whether the approval of the application, on balance, is in the public interest. An application for a

bypass competitive rate will be approved only if such a rate is found by the Board to be in the public interest.

5.0.23 Public interest is a fluid concept and its application as a legal standard depends on the facts and the circumstances existing at the time of the application. It is not possible to compile a list of all the criteria that might make up the public interest from time to time. The question of public interest is not a question of fact, but it is a question of judgement based on the facts and circumstances before the Board. Since facts and circumstances change from case to case, so will the depiction of the public interest.

5.0.24 The Board has found in past decisions that postage stamp rates serve the public interest. The Board discussed the concept of postage stamp rates in the T-Rates Decision and stated in the CP Forest Decision that:

Postage stamp rates within each class of customers are the accepted norm in Ontario and the Board will not depart from this principle in favour of distance related rates unless there are valid and compelling reasons to do so.

The Board in the CP Forest Decision identified this concept of postage stamp rates as being one of the key principles in deciding if the public interest is best met by approving a bypass competitive rate for an individual customer.

5.0.25 In addition to postage stamp rates, the rate structure in Ontario is based on the principle of class ratemaking, where customers with common characteristics are grouped together and treated similarly. The granting of a bypass competitive rate marks a departure from this principle.

5.0.26 Class ratemaking and postage stamp rates are the accepted rule in Ontario. There are exceptions to the rule; but these were approved only after due consideration and an examination of the facts and circumstances

surrounding the request for the exception and the public interest. There is a burden of proof on an applicant to show why it should be outside the class rate system and obtain a special rate. Since a bypass competitive rate is a special rate, an applicant must address both the private and public interest considerations (the former being a subset of the latter), for in the end, the application is granted on public, not private, interest grounds.

5.0.27 There was a suggestion by Cardinal Power in this proceeding that it would be unjust, unreasonable and unduly discriminatory to deny the Rate Application given the decisions in C-I-L and Nitrochem. Although the Board notes that in those cases the bypass competitive rates were found to be in the public interest, the public interest considerations used by the Board to arrive at its conclusions were not set out in any definitive way in the reasons for the decisions.

5.0.28 The Board did discuss, however, public interest criteria in more detail in both the Northland and CP Forest Decisions. In the Northland Decision the Board found the applicant not to be a credible bypass candidate, and although it was not necessary to deal with public interest considerations, it did go on to expound on some of those that it considered relevant. The Board indicated that an applicant for a bypass competitive rate would need valid, compelling reasons to persuade the Board to depart from the traditional postage stamp rates. The Board stated that there was a heavy onus on an applicant to satisfy the Board that such a rate was an appropriate response to the applicant's "problem". The Board was of the view that increased profit was not a compelling reason. This was the first time that the requirement for the transportation service was incremental, and therefore, there was no concern over a duplication of facilities.

5.0.29 The Board in the CP Forest Decision was quite detailed as to the public interest criteria it viewed as relevant in that case. The Board regarded the approval of a bypass competitive rate as a serious issue and termed such a rate as being "beyond the ordinary." The Board determined that an

applicant has an onus to demonstrate an "extraordinary reason", an economic justification, for the rate. The Board wanted to be satisfied that the rate was the appropriate response to the applicant's "problem". In this regard, the Board specifically referred to a notion of "economic threat" on the part of the applicant (i.e., its economic viability) and to the threat of load disappearing from the system (i.e., lost revenue to the utility). In the Board's view, the applicant had to show a valid and compelling reason that is more than "a simple cost reduction" to justify a departure from postage stamp rates. Where costs savings are the reason for the application, the Board indicated that it wanted to see the magnitude of the saving in relation to the goal of reducing costs and to the total annual cost of operations. It also indicated that the cost shifting consequences of granting a bypass competitive rate had to be justified since the granting of a bypass competitive rate would result in burdening other customers with extra costs. In the CP Forest case, the Board found no economic threat nor any real danger that the system would lose the load. It also considered the shifting of costs (CP Forest being an existing customer) to other customers as a negative impact outweighing the benefits to the applicant. The Board found that a bypass competitive rate was not in the public interest in that case.

- 5.0.30 There have been submissions made that there is no cost shifting where the customer is incremental. The Board does not agree. In the Board's view, where the load is incremental there is notional cost shifting. Assuming Centra is serving Cardinal Power at the special rate, industrial customers will pay \$0.12 per 10³m³ more than if Cardinal Power was paying the class rate. That is not to say that cost shifting is the only determinant of the application. In fact, that is not the case; in the decisions dealing with Cyanamid, Nitrochem and C-I-L the Board accepted the cost shifting consequences caused by the bypass competitive rate. Cost shifting is only one item that the Board must consider.

- 5.0.31 Cardinal Power testified that a bypass competitive rate would result in cost savings, which would reduce its risk exposure, particularly given the nature of its front-loaded contract with Ontario Hydro. The Board finds that these costs savings enjoyed by the Applicant would result, assuming that Cardinal Power is on the Centra system, in a reduction of the rate benefits that other Rate 20 customers would obtain by having a large incremental customer joining the class. The Board regards this circumstance as notional cost shifting. Is this cost shifting a burden? Although it may not be a burden in the short-term, nor in the classic sense of the word, it certainly skews the system, all for the benefit of a private interest, with no obvious counter-balancing public interest benefit.
- 5.0.32 The characteristics of the Applicant would place it in the Rate 20 class, and Rate 20 is higher than the requested bypass competitive rate. Is the proposed rate unfair or unduly discriminatory compared to the rate paid by Rate 20 customers? Assuming that Cardinal Power is on the Centra system, other customers would be better off if the Applicant is a Rate 20 customer and they would, as a class, realize the maximum advantage from the Applicant paying the class rate. There would be no discrimination amongst Rate 20 customers as all such customers would be treated the same.
- 5.0.33 Is the Applicant's reason for the request, its need to improve its risk factors, a valid, compelling reason? Although the Board acknowledges the Applicant's concern for risk reduction, the Board is not convinced Cardinal Power's need to reduce its risk exposure at this time is such that the Board should allow a departure from the rule of class ratemaking and postage stamp rates. The Board does not consider the Applicant as being disadvantaged by being placed in the Rate 20 class and notes that it presented its financial analysis to its lender on the assumption that Rate 20 was in effect.

- 5.0.34 The issue of bypass is an important one that directly affects the economic well-being of a potential bypass customer, all other customers on the utility's system, and the system itself. The gas distribution system in Ontario has been treated as an integrated system, and all customers of a utility have come to expect that they will share in the costs and benefits of that integration. If that is to change, it should be done on some significant public interest principle sufficient to counterbalance the expectations of the continuance of an integrated system.
- 5.0.35 One of the circumstances that the Board took into its consideration in this case is the unique characteristics of the Centra system. First of all, the major industrial customers on the Centra system are a significant customer class in terms of their volume compared to the residential customer class. Second, many of these industrial customers are in close proximity to the TCPL transmission lines. These characteristics increase Centra system's vulnerability to bypass.
- 5.0.36 As Board Staff pointed out, it is inevitable that rates will be higher than stand-alone costs for some customers and lower for others, in that postage stamp rates reflect the average of costs and return for all the customers of a particular rate class. The Board views the payment above real costs as a contribution to the integrity of the gas distribution system. This contribution is the price of conserving an integrated structure that has been established as reflective of the broad public interest.
- 5.0.37 The granting of a bypass competitive rate is the first step in the erosion of a system based on class ratemaking and postage stamp rates, a system that has been determined to be in the public interest. This is not a step that this Board takes lightly. The Board will approve special rates if it is presented with compelling reasons that would satisfy the Board that the special rate would best serve the public interest. The Board is not convinced that the public interest is best served by granting a bypass competitive rate to Cardinal Power at this time.

5.0.38 The Board continues to be guided by the findings in the Bypass Decision as they pertain generally to bypass application:

1. As a general policy, physical bypass of the LDC for the transportation of gas is available where it is in the public interest.
2. Each application for physical bypass will be considered on the basis of its individual merits.
3. The Board will rely on a very broad definition of the public interest.
4. The Board encourages ratemaking alternatives to bypass.

5.0.39 On the basis of the fourth principle Centra and the Applicant entered into negotiations resulting in this Rate Application. In light of the evidence heard in this proceeding, the Board would augment this last principle to add two other considerations to better guide both potential applicants for bypass competitive rates and the utility in this matter:

4. The Board encourages ratemaking alternatives to bypass.
 - a) Class ratemaking techniques are to be explored.
 - b) A customer specific rate should be considered only as a last resort.

5.0.40 The Board heard that there was a certain level of discontent with the present structure of Rate 20, and it seemed that Centra was not dealing with those issues on a timely basis. This posed a dilemma for the Board as it knew that rejecting the Rate Application would result in placing the Applicant in Rate 20, a potentially problematic rate class.

- 5.0.41 The Board has since become aware that Centra recently filed its 1994 rates application, under Board File No. E.B.R.O. 484, and has included a proposal to create a high volume, high load factor rate class. If the proposal is accepted by the Board, customers like Cardinal Power may observe some rate relief. This approach also recognizes the aforementioned principle that class ratemaking techniques should be examined (and exhausted) before developing a customer specific rate in addressing potential bypass. The Board only comments that it would have hoped that Centra could have been more forthcoming about its intent in this regard in this proceeding, and perhaps less supportive of a deviation from class ratemaking and postage stamp rate principles than it was in its support of the Rate Application.
- 5.0.42 The Board does not approve a bypass competitive rate for Cardinal Power. In the Board's view the Applicant did not pass the three-part test. Although Cardinal Power may be a credible bypass candidate, the Board is not satisfied that it is in the public interest to grant this special rate to the Applicant under the circumstances.

DECISION WITH REASONS

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6. COSTS

6.0.1 Section 28 of the Act authorizes the Board to award costs of and incidental to any proceeding before it. The Board's draft Rules of Practice and Procedure and Cost Award Guidelines, as amended effective January 1, 1993, set out the procedures applicable to cost awards. Costs may be awarded to an intervenor who the Board believes:

- has or represents a substantial interest in the proceeding to the extent that the intervenor or those it represents will be affected beneficially or adversely by the outcome,
- participates reasonably in the proceeding, and
- contributes to a better understanding of the issues by the Board.

6.0.2 IGUA and Northland applied for an award of costs in this proceeding.

Positions of the Parties

6.0.3 IGUA submitted that it participated actively and reasonably in the proceeding. It maintained that the supplementary responses to interrogatories provided by the Applicant in response to the Board's disposition of IGUA's motion shortened the time required for the

examination and cross-examination of witnesses from Cardinal Power and Centra. IGUA requested that the Board find that its participation was reasonable and of assistance to the Board and justifies an award of 100 percent of its reasonably incurred costs.

- 6.0.4 Northland submitted that it is entitled to costs because: it is directly affected by the Rate Application; it has a unique contribution to make as it is a Rate 20 customer, a potential physical bypass or bypass competitive rate candidate, and a competitor of Cardinal Power; its intervention has been constructive, "as evidenced by its support of the Cardinal Power Application"; and it has conducted its intervention in an efficient and economic manner.
- 6.0.5 Northland was granted late intervenor status at the outset of the hearing. At that time, Counsel for Cardinal Power did not object to giving status to the late intervenors (Northland and Destec), but submitted that they should do so at their own cost. Northland did not object to this submission of Counsel. In its written argument, however, Northland claimed that the Applicant was penalizing a late intervenor by its submission advocating the denial of costs. Northland submitted that there is no linkage between a late intervention and costs, particularly where the late intervention has not caused prejudice to anyone, including the Applicant, and where there was good reason for the late intervention.
- 6.0.6 In terms of the assessment of the costs claimed, the Applicant requested that the Assessment Officer ensure that costs incurred related "to attendances in connection with other simultaneously held proceedings (such as the Union case, E.B.R.O. 476) be fairly allocated to those proceedings."

Board Findings

- 6.0.7 The Board has considered the submissions and conduct of the cost applicants. The Board is also cognizant of the financial liability that the Applicant exposes itself to in its efforts to demonstrate responsible management in a regulated environment. The Board acknowledges the Applicant's status, as noted in its Reply, as a private entity that has no cost of service over which it may spread the cost awards arising from the proceeding.
- 6.0.8 IGUA has a substantial interest in this proceeding. IGUA is an association that represents industrial gas users, some of which are served by Centra under Rate 20. Its positions on physical bypass and bypass competitive rates are well-documented. From the Board's perspective, Counsel for IGUA positioned IGUA during the hearing as an opponent of bypass and bypass competitive rates. Although the witness for IGUA admitted that bypass was possible, he testified that he found it difficult to imagine when it would occur. Further, with respect to bypass competitive rates, he testified that, although possible, based on IGUA's reading of the CP Forest Decision, such a rate is not attainable.
- 6.0.9 In the Board's view time spent advocating general opposition to bypass competitive rates, in light of the Board's policy that such rates are available, is not time well spent in the hearing and did nothing to help the Board resolve the meaning and scope of the public interest component of this application. Although IGUA facilitated the hearing process by bringing its motion and provided some assistance to the Board in its understanding of the issues, the Board did not find that IGUA's participation in total assisted the Board such that IGUA should receive 100 percent of its reasonably incurred costs.
- 6.0.10 The Board finds that IGUA is entitled to an award of costs and, having regard to the circumstances of its intervention, the private status of the

Applicant, and the results of this proceeding, the Board finds that IGUA should assume some of its own costs in this proceeding. The Board awards IGUA 66 percent of its counsel's fees and 100 percent of all reasonably incurred disbursements (including those of counsel), subject to the Board's assessment process.

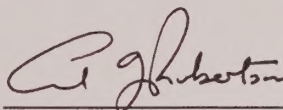
6.0.11 The Board is aware of Centra's position that it will negotiate a bypass competitive rate with potential bypass candidates and support the rate in the context of an application before the Board, on the condition that it is not exposed to costs of the proceeding. Since the Board regards Centra as being answerable for the state of the Rate 20 class, and the controversy surrounding that class is, for the main part, a motivation for special rates, the Board finds that Centra should bear some responsibility for the costs flowing from this proceeding. If the contentions had been settled or the rate class justified, or at the very least, if Centra had been more definite about having that matter resolved on its own motion in its next rates proceeding at the time of this hearing, then the Board would not have been so inclined. The Board finds that Centra shall bear a portion of the costs awarded to IGUA. The Board finds that Cardinal Power and Centra shall equally share the liability for the costs awarded to IGUA.

6.0.12 Cardinal Power conditionally accepted Northland's late intervention, namely, that Northland should bear its own costs. Although Northland was not asked expressly by the Board whether it accepted that condition, the Board regards the onus as being on Northland to have either objected to the condition or provided comment in the hearing, where the Board would have had the opportunity to hear the parties make full submissions on the issue for determination at that time. The Board finds that, effectively, Northland accepted Cardinal Power's condition in proceeding as an intervenor without objection or comment until its Argument. In any event, even if the Board had not found Northland to be estopped from pursuing an application for costs, the Board would not have found Northland to be eligible for a cost award. The Board is of the opinion that Northland did

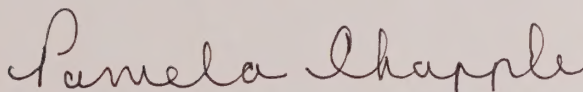
not contribute to a better understanding of the issues by the Board. Its intervention was wholly self-serving and added no substance to the Rate Application. In either case, the Board denies a cost award to Northland.

- 6.0.13 The Board directs Cardinal Power and Centra to each pay an equal share of the costs awarded to IGUA immediately upon receipt of the Board's Cost Order. The Board also directs Cardinal Power to pay the Board's costs of and incidental to this proceeding immediately upon receipt of the Board's Cost Order and invoice.

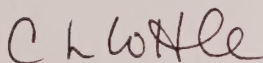
DATED AT Toronto May 27, 1993.



E.J. Robertson
Presiding Member



Pamela Chapple
Member



C.L. Cottle
Member

